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SUBJECT: CONSUMPTION LAGGING IN HUBEI'S NEW COUNTRYSIDE

SUMMARY

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11. (SBU) In rural Hubei Province, incomes remain low and government policies have failed to boost consumption, according to Provincial Government officials. Local governments are facing a financial crunch due to loss of tax revenue and increasing pressure to provide compensation to farmers for land that is seized for public works and development projects. Hubei's economy is still highly agricultural, but non-farm income earned in Wuhan, other Hubei cities, and in China's coastal areas is increasingly important. Efforts to launch the Central Government's New Socialist Countryside initiative have been largely limited to training local officials and building model villages.  
END SUMMARY.

TRAVEL TO HUBEI

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12. (SBU) Econ Macroeconomic Unit Chief, Econoff, Econ Assistant, and Conoff traveled to Wuhan, Hubei Province, from October 31 to November 2. Emboffs met with Provincial Government officials at Hubei's Development and Reform Commission, Foreign Affairs Office, Bureau of Land Resources, Statistics Bureau and Academy of Social Sciences. They also discussed rural issues with an American businessman who sells wind turbines in rural Hubei and the Assistant Mayor of Chi Bi City.

SHARE OF INCOME FROM NON-FARM ACTIVITIES INCREASING

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13. (SBU) Hubei's rural residents derive a growing share (approximately 40 percent) of their income from non-farm sources, according to Sun Xiaohong at the Hubei Provincial Development and Reform Commission (HPDRC). Many of Hubei's rural residents have migrated to factory jobs in Guangdong Province, Fujian Province, and Shanghai and their remittances remain an important contributor to rural incomes, Sun said. A researcher at the Hubei Academy of Social Sciences (HASS) said that he believes the number of farmers moving to the cities is growing rapidly.

14. (SBU) Remittances notwithstanding, Hubei's rural per capita income is RMB 3099 (less than USD 400), below the

national average rural income of RMB 3254. Low incomes and high precautionary savings mean that one year after the Central Government launched the New Socialist Countryside initiative to improve living standards in non-urban areas, Hubei's Provincial Government is struggling to achieve its goal of boosting consumption in rural areas, according to Sun. The HASS researcher added that a stark contrast exists between Wuhan, which is attracting large international retailers such as Wal-Mart, and Hubei's countryside, where branded companies are unwilling to venture due to a low rate of consumption.

#### HUBEI'S NEW COUNTRYSIDE PROMOTING MODELS OVER SUBSTANCE

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15. (SBU) Hubei's top economic priority in 2006 was the improvement of rural livelihoods, with extensive focus given to training local government officials on rural policy and social service delivery. The province placed even greater emphasis on building 500 model villages in Hubei Province to exhibit high standards of health and sanitation, education, and culture and demonstrate an overall improvement in farmers' livelihoods, Sun said. HPDRC coordinates government bureaus' model village projects, but Sun could not say what percentage of the Provincial Government's New Countryside budget is allocated to model villages. (Note: The day after we met with Sun, an editorial in the China Daily criticized model villages as an example of local government leaders looking for "political achievements to boost their chances of promotion (and) make profit for themselves." End Note.)

#### PUBLIC FINANCE CRISIS LOOMING

BEIJING 00023786 002 OF 002

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16. (SBU) Sun said that Provincial Government officials face a looming public finance crisis created by the elimination of the agricultural tax for rural residents. Consequently, county governments in Hubei Province, like counties in other areas of China, are contending with a drop in tax revenue without a parallel reduction in obligations to provide increased social services such as health care and education that are important components of the Central Government's New Socialist Countryside initiative. Wu Zhengyu, Assistant Mayor of Chi Bi City near Wuhan, told Econoff that the public finance crunch is particularly acute in the rural areas of his district and is a common problem at the grass-roots level. The elimination of the agricultural tax has benefited farmers and attracted back to the countryside many rural dwellers who had temporarily left their farms, but now local governments lack funds to provide services, and there are no signs that the Central or Provincial Government will provide additional funding to make up the shortfall.

#### HUBEI'S LAND COMPENSATION DILEMMA

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17. (SBU) Another factor in Hubei Province potentially threatens to exacerbate the government's financial shortfall. According to Provincial Government officials, compensation required for farmers from whom government bureaus seize land for public works and development projects is likely to increase rapidly. Zhang Jianren, Vice Director, Hubei Provincial Bureau of Land Resources, cited three reasons for the disproportionate pressure on Hubei to offer land compensation to rural residents:

--the Provincial Government's intention to abide by the Central Government's recently announced directive on compensation for hydropower and water projects and provide the maximum level of compensation to farmers;

--the Provincial Government's plan to increase the

province's urbanization rate to 50 percent by the end of the Eleventh Five-Year Plan (in 2010), which will require a significant number of new road and water projects that will necessitate additional land seizures; and

--the continued pressure on local government officials in Hubei Province to follow through on resettlement commitments to the 260,000 people relocated by the Three Gorges Dam project in the western part of the province.

COMMENT

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18. (SBU) What we saw is in line with the views of many observers: Wuhan, China's fifth-ranked city by population, is enjoying sufficiently rapid growth and investment so as to possibly join Beijing, Shanghai, and Guangzhou as one of China's few first-tier cities. The expansion of Wuhan and nearby up-and-coming cities in Hubei like Chi Bi is an important adjunct to the coastal cities for the countryside's excess labor supply. Reliance on this kind of successful urban growth is likely to continue -- policies to promote rural-urban balance notwithstanding -- because efforts to boost standards of living and consumption in the countryside are clearly flagging.

RANDT